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Summary

The present report provides a detailed overview of UNCDF performance in 2006 in terms of programme, management and financial results. The results are consistent with the managing-for-results strategy set forth in the UNCDF business plan approved by the Executive Board for 2006-2007. With an overall performance rate of 82 per cent in its local development practice area and 78 per cent in its microfinance practice area, UNCDF fully achieved its programmatic results and outcomes. Target achievement in both practice areas was considerably above 2005 levels. UNCDF also substantially achieved all its management and financial results in 2006, with the exception of total income from core and non-core resources. While total resources increased by 11 per cent, this increase not sufficient to reach the 2006 resource mobilization targets set in 2005. UNCDF was able to accomplish the development, management, and financial results set forth above while sustaining its liquidity and financial soundness.

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Introduction

1. The United Nations Capital Development Fund (UNCDF) makes investments in the least developed countries (LDCs). Its overall goal is to reduce poverty in the LDCs and to help them achieve the Millennium Development Goals (MDGs). It does so by investing in two practice areas – local development and microfinance – while striving to strengthen organizational performance. The three sub-goals of the UNCDF strategic results framework, as included in the UNCDF business plan 2005-2007, capture these performance dimensions.

2. The present report provides an overview of UNCDF performance in 2006 for each of the sub-goals, within a continuously changing internal and external environment. The format of the report, which was revised in 2005 to be consistent with the reporting framework used by UNDP, has remained unchanged.

3. 2006 was a transition year for UNCDF. It represented the first full year after the organizational restructuring and change management process, begun in 2005, and it was the second year of the implementation of the business plan approved by the Executive Board in June 2005. It was the first year in which the UNCDF administrative budget was mainstreamed into the UNDP biennium support budget. UNDP and UNCDF have worked constructively and collegially during the year to advance their strategic partnership arrangements, culminating in a joint presentation to the Executive Board at its first regular session 2007. Internally, the significant reorganization of UNCDF that started in July 2005 was completed, with the reduction of headquarters staffing taking effect and the regional presence of UNCDF substantially expanded.

4. The present report focuses, in three chapters, on the programme, management, and financial results achieved in 2006 in implementing the business plan. The report then links the development results to the framework proposed for the UNDP strategic plan, 2008-2011.

I. Programme results

A. Performance analysis for sub-goal 1: local development

5. The UNCDF local development practice area is concerned with building the capacity of local governments and other local stakeholders to foster participatory local development. The underlying theme is one of decentralization reforms that enable local governments to deliver capital investment for pro-poor infrastructure and services to rural communities, thus supporting the achievement of the MDGs at the local level.

6. All UNCDF local development programmes pilot institutional reform at the local government level, using modest capital funding as an incentive for change. This emphasizes the importance of the investment mandate of UNCDF, which allows it to go beyond normal capacity-building activities to focus on establishing and supporting new systems, procedures and capacities for local government operations. Piloting gives the opportunity to governments and local authorities to undertake 'real time' planning and implementation, and to generate lessons and learning, which are critical for policy impact and replication.

7. In 2006, UNCDF had ongoing local development programmes and local development funds in 23 LDCs, with support to ten more LDCs being prepared for start-up in 2007. Overall, the performance was most satisfactory with a rate of target achievement of 82 per cent and an average delivery against available core resources of 84 per cent.

8. The highlights of 2006 results in this practice area are:

(a) UNCDF piloting was successful in helping shape national programmes on decentralization and local development in a number of countries. Those national programmes increasingly are supported by donors in a coordinated fashion. Some examples follow:

(i) In Bangladesh, the Government approved a more than $200 million 'local government support programme', replicating the UNCDF/UNDP pilot and scaling it up to 4,500 Union Parishads. The World Bank, the European Commission, the Danish International Development Association and, earlier, the Sustainable Development Commission, joined UNDP and UNCDF to support this national programme.

(ii) The Nicaraguan Government adopted its 'national strategy for decentralization and local development' based on the UNCDF local development model. The United Nations Resident Coordinator, with UNCDF technical support, now seeks to align and harmonize United Nations and development partner support for this national strategy.

(iii) In Mozambique, UNCDF, UNDP, the World Bank and the German Agency for Technical Cooperation recently jointly evaluated their prior local development collaboration and used those results to advise the Government on a new national decentralized planning and finance programme. The Government has decided, in principle, to establish the programme with a resource-pooling or common-funding arrangement to guide donor support. The programme will draw upon lessons learned from the UNCDF/UNDP pilot local development programme, which has been implemented successfully in Northern Mozambique.

(b) UNCDF also achieved several significant successes in 2006 in terms of scaling up its pilot experience with local development programmes and replicating this experience in partnership with other development partners. Some examples:

(i) In Benin, the UNCDF 'decentralization and local development' pilot pioneered a public expenditure management process using the National Treasury to channel investment funding. The Government and several development partners agreed to replicate and scale up the UNCDF model to additional provinces.

(ii) In Yemen, coverage of the 'decentralization and local development support programme' continued to expand and reached 48 districts (from the original six in 2003). Nine donors have harmonized their approach and pooled their funding in a UNDP/UNCDF-led support programme that now exceeds $12 million.

(iii) The 'decentralized financing and development programme' in Nepal, covering 20 districts, was able to continue funding and supporting local-level investments during the recent political upheavals. The Government recently adopted the performance-based grant policy piloted by UNCDF. The programme is emerging as a national model, on the basis of which the next phase programme will be designed. That new programme will be supported jointly by UNCDF, UNDP, the Department for International Development, the Netherlands Development Organization and the Norwegian Agency for Development Cooperation.

(c) UNCDF is increasingly taking an important role in coordinating development partners to support national decentralization and local development programmes in post-conflict countries such as the Democratic Republic of the Congo, Liberia, Sierra Leone and Timor Leste. The programmes are in line with the growing UNDP and UNCDF emphasis on supporting local governments as key local recovery institutions.

Table 1 Achievements of 2006 targets for the local development practice area

Core results and outcomes	Overall target achievement in 2005 (%)	Overall target achievement in 2006 (%)	Performance achieved
Core result 1: Pilots for public expenditure management infrastructure and service delivery (ISD) successfully implemented			
Outcome 1.1: Effective, participatory assessment of demand for ISD by local governments in UNCDF pilots	93	92	Fully achieved
Outcome 1.2: Increased expenditure on ISD effectively, equitably and transparently managed by local governments in UNCDF pilots	73	78	Fully achieved
Outcome 1.3: Increased more effective supply and maintenance of basic socio-economic infrastructure and services by local governments, service providers and local communities in UNCDF pilots	76	90	Fully achieved
Outcome 1.4: Sustained management of the local natural-resource base ensured by local governments in UNCDF pilots	58	67	Partly achieved
Outcome 1.5: Enabling environment for local economic development established by local governments in UNCDF pilots	*	*	
Core result 2: Pilot models and lessons leveraged for policy impact and replication			
Outcome 1.6: Government amendments to policy/legal/regulatory frameworks reflect lessons from UNCDF pilots	91	75	Fully achieved
Outcome 1.7: UNCDF pilots scaled up through replication by other funding entities and/or government budgetary resources	48	92	Fully achieved
Total	**72**	**82**	**Fully achieved**

Data source: UNCDF MIS data from 20 programmes

* Outcomes for which no targets had been set in 2006, but for which targets will be set in 2007.

9. UNCDF achieved an overall performance rate of 82 per cent (table 1) and thus fully achieved its core results and outcomes in its local development practice area in 2006. 2006 performance represented an improvement of 10 per cent compared to 2005. In terms of capacity-building of local governments, the high 2005 performance level for testing and institutionalization participatory planning (outcome 1.1) and public expenditure management systems (outcome 1.2) was maintained. Nevertheless, the consistency of the local development plans with sectoral and higher-level planning (such as regional, provincial, and poverty-reduction strategies) is still a huge challenge for the local planning process. The performance on the outcomes dealing with investments in service delivery (outcome 1.3) and natural resources management (outcome 1.4) improved by 14 per cent and 9 per cent, respectively.

10. The targeted results were fully achieved in the area of policy impact (outcome 1.6) and replication (outcome 1.7). While performance in reaching policy impact was 75 per cent of the planned targets in 2006 (against 91 per cent in 2005), UNCDF achieved 92 per cent of targets for replication of UNCDF best practices in 2006, compared to 48 per cent in 2005. Achieving tangible results in those two areas is a critical priority for UNCDF, as these results demonstrate programme effectiveness at the country level. The two areas remain extremely challenging for UNCDF, but the good results reflect the accumulation of several years' worth of work on the ground, at the country level.

11. The absence of reporting on outcome 1.4: local economic development reflects the challenges that UNCDF faced in starting up pilot activities during 2006. This was due to limited human and financial resources to be devoted to this new programmatic area. Another area of disappointing results has been the relatively slow progress towards a more systematic exploitation of potential synergies between the microfinance and local development practice areas through joint innovations on the ground. It is expected that 2007 will show an improvement in both areas.

12. Table 2 provides an overview of results achievements during 2006 with respect to the outreach of UNCDF local development investments. As the table highlights, approximately 3.6 million rural people were reached through the provision of local service delivery during 2006. UNCDF provided investment resources for 1,775 small-scale infrastructure projects, through 437 local governments during the year. This is an average of 81 investments per country, or four for each client local government.

Table 2. Outreach of UNCDF local development investments during 2006

	No. of countries	Local gov'ts supported	Avg. local gov'ts per country	No. of projects	Beneficiaries (millions)
West Africa	7	180	26	513	0.5
Eastern/Southern Africa	7	63	9	165	1.4
Asia (includes Yemen)	6	147	24	1,040	1.6
Latin America	2	47	23	57	0.1
Total	**22**	**437**	**20**	**1,775**	**3.6**

Data source: UNCDF MIS data from 20 programme (countries without capital investments in 2006 excluded).

13. Table 3 shows how capital grants were used in terms of completed projects in 2006 and their sectoral distribution in 16 of the programmes on which data were received. In comparison with 2005, the total number of investments completed by the end of 2006 decreased 33 per cent, while the average value of an investment increased by 62 per cent. The larger size of investments seems to indicate a longer construction period, with a good number of projects started in 2006 only scheduled for completion in 2007. Overall, the average investment per capita increased from $2.10 to $2.32.

Table 3. Expenditure and types of local development investments during 2006

Type of investment	No. of projects	Investment (in $ millions)	Average unit cost (in dollars)	Percentage of projects (% investment)
Education	275	1.76	6,400	21 %
Health	120	1.22	0,166	14 %
Water supply	284	2.31	8,134	28 %
Local government offices, community facilities	205	0.51	2,487	6 %
Markets, agriculture, natural resources management	405	1.91	4,716	23 %
Roads, bridges, culverts	413	0.65	1,574	8 %
Total	**1,748**	**8.36**	**4,782**	**100%**

Data source: UNCDF MIS data from 16 programmes. Accurate user rates available from 8 programmes. Other programmes estimated.

14. Water supply, rural economic activity and education each accounted for more than 20 per cent of UNCDF investment resources in 2006. These were followed by health (14 per cent), roads, bridges and culverts (8 per cent), and facilities (6 per cent). As in 2005, more than 60 per cent of all investments were dedicated to enhancing access to social services and infrastructure, whereas about a quarter of UNCDF investment in 2006 was used for economic capital formation. Ultimately, all of these investments are devoted to pro-poor and gender equitable local development investment and support the achievement of the MDGs at the local level. The UNCDF working paper *Gender Development: Investment Methods for Greater Equity* provides more information on how UNCDF intends to better mainstream issues of gender equality and women's empowerment within its local development programmes.

15. Healthy local government finances are crucial for the long term sustainability of the results produced in UNCDF local development programmes. To achieve this sustainability, a good mix is required of the three sources that make up local income: fiscal transfers, local revenue and donor support. Further, on the expenditure side local governments need to appropriately share total income to fund both their recurrent and investment budgets. The next paragraphs summarize a special analysis carried out for the purposes of this report to evaluate the longer-term results of UNCDF interventions in strengthening local finance.

16. While outcome 1.2 showed a fully satisfactory performance, the indicators contributing to this outcome provide a more detailed picture. In 2006, UNCDF-supported programmes had good results on the income side: they exceeded their targets for the successful management of inter-governmental transfers and their planned increase of local revenue per capita through tax collection, contributions, and cost recovery. On the expenditure side, however, the programmes reported that they were only partially achieving projected increases for budget to be invested in basic infrastructure and social services.

17. The results in tables 4 and 5 partially confirm this tendency when comparing 2006 results with the results over a five-year period. Based on the financial data for nine countries, it can be concluded that the interventions by UNCDF in fiscal transfer and local revenue mobilization, from both policy and practical perspectives, seem to have a direct and positive impact. In 2006, 53 per cent of local government income, on average, was derived from national income sources, equally divided between fiscal transfers and local revenue. Donor support for investments made up only 47 per cent of total income.

Table 4. Actual income sources of local governments (average per programme, in dollars)

Income sources	2002	%	2003	%	2004	%	2005	%	2006	%
Fiscal transfer	$ 23,450	5	$ 92,787	12	$ 324,300	32	$ 71,794	12	$236,261	26
Local revenue	102,878	22	185,555	23	413,796	40	169,852	29	244,610	27
Donor support	340,669	73	521,449	65	276,056	28	352,596	59	438,269	47
Total	**$466,997**	**100**	**$799,791**	**100**	**1,016,157**	**100**	**$594,242**	**100**	**$919,140**	**100**

Data source: UNCDF MIS data from a total of 6 countries (2002 – 2004) and 9 countries (2005-2006).
For countries without budget closure, figures are estimates (2006).

18. Table 5 provides indicative data regarding how available local government budgets were used for recurrent expenditures and investment purposes. In 2006, 58 per cent of total local government budgets in UNCDF programme countries was used for local investments and 42 per cent for recurrent expenditures. More detailed analysis of data sources reveals that 100 per cent of donor funding to local governments was used to fund investments and 34 per cent of local income and fiscal transfers was used for the same purpose. Approximately 66 per cent of local income and fiscal transfers was used to cover recurrent costs. In fact, 2006 was the fourth consecutive year in which recurrent expenditures increased as part of the total budget. This trend needs to be monitored and analysed carefully so as to ensure that local authorities supported by UNCDF are moving towards an appropriate

balance with regard to recurrent costs and investments as a share of local income and fiscal transfers, while reducing their dependence on donor resources.

Table 5. Recurrent and investment budgets of local governments (average per programme in dollars)

Budget categories	2002	%	2003	%	2004	%	2005	%	2006	%
Recurrent	$ 85,176	19	$197,070	25	$310,335	31	$191,855	33	$387,761	42
Investments	381,821	81	602,721	75	703,817	69	402,387	67	531,379	58
Total	**$466,997**	**100**	**$799,791**	**100**	**1,016,157**	**100**	**$594,242**	**100**	**$919,140**	**100**

Data source: UNCDF MIS (same data material as Table 4)

19. To conclude, the demand for decentralization and local development investment – and supporting advice – is high in all regions where UNDP has programmes. Decentralization and local development are closely linked to the democratization process, which many of the developing countries are undergoing. Decentralization and local development are also central to the localization of the MDGs and, indeed, to the vision, values and principles of the United Nations. They have a broad appeal and interest among governments, development partners and associations of local governments. As a result, the UNDP strategic plan, 2008-2011, reflects the joint intention of UNDP and UNCDF to focus even more strongly on strengthening the capacities of local governments and other stakeholders to foster participatory local development and support achievement of the MDGs.

B. Performance analysis for sub-goal 2: microfinance

20. In its microfinance practice area, UNCDF supports the development of inclusive financial sectors that provide a broad range of affordable financial services to poor and low-income families and small and micro enterprises in the LDCs, on a sustainable basis. This is an effective means of contributing to poverty reduction and to achievement of the MDGs.

21 In 2006, applying its sector development approach, UNCDF expanded its inclusive finance programme to additional LDCs, in line with the goals set forth in the UNCDF business plan. UNCDF formulated five new inclusive finance programmes, bringing the number of LDCs applying its sector development approach to 11, nine of which are in Sub-Saharan Africa and two in Asia. A number of additional countries in Africa, the Arab States and Asia have requested UNCDF assistance in building an inclusive financial sector, which should result in 16 LDCs' benefiting from UNCDF support by the end of 2007.

22. Highlights of 2006 results achieved in this practice area were:

(a) Initial indications of the results of the sector development approach to financial inclusion are encouraging, as the Sierra Leone case illustrates. Sierra Leone undertook the first inclusive financial sector programme that UNCDF piloted. The programme began in 2003 and was submitted to a joint mid-term evaluation in 2006. The independent evaluation concluded that "the evaluation findings indicate that the project is on track with regard to increasing sustainable access to financial services for poor and low-income people, as measured by the indicators cited below." "It is clear that the project is well on the way to achieving its targets, having achieved or surpassed most of its mid-term goals. The project has generated the following results at the micro or retail level as of September 2006:

(i) There are 42, 768 active clients being served by nine microfinance institutions (MFIs)
(ii) Five MFIs report more than 100 per cent operational self – sufficiency
(iii) One MFI has branches in seven towns and seven sub-branches in surrounding areas
(iv) One MFI is in the final stages of negotiations with a major international investor
(v) One new donor has joined the Investment Committee
(vi) $3.88 million additional resources have been mobilized for the project."

"Additionally, progress has been made on establishing and strengthening local structures at the meso (support infrastructure) and macro (policy) levels, particularly through support to the Bank of Sierra Leone (Central Bank) and the Sierra Leone Association of Microfinance Institutions (SLAMFI)."

(b) In terms of outreach (outcome 2.1), more than 616,000 clients, 66 per cent of whom were female, received microfinance services from 28 financial service providers (FSPs) supported by UNCDF in 2006. The FSPs include non-bank financial institutions, credit unions, microfinance institutions and community banks. Moreover, almost 90% of FSPs supported by UNCDF had an average loan size smaller than the gross domestic product per capita, which shows an effective poverty targeting by the majority of the FSPs funded by UNCDF.

23 UNCDF achieved an overall target achievement rating of 78 per cent in 2006 in its microfinance practice area (table 6). Thus, its performance targets for the year were fully achieved. In terms of outreach (outcome 2.1), the 28 FSPs reporting collectively exceeded their growth targets by 30,000 clients. From a baseline of 379,018 clients in 2004 and 438,272 in 2005, the number of active clients at the end of 2006 amounted to 616,035. The increases over 2004 and 2005 are respectively 62.5 per cent and 40.6 per cent.

24. Results on sustainability and efficiency for microfinance institutions and other FSPs were below expectations (outcome 2.3). Out of eight FSPs with reported results for 2006, 50 per cent met their targets for profitability and are on the path to financial sustainability. The FSPs with higher profitability tended to be older institutional investments in West Africa, confirming that UNCDF is taking risk and investing in younger, unproven institutions. Only 39 per cent of the FSPs supported by UNCDF meet the international standard of strong portfolio quality (portfolio at risk at 30 days of less than 5 per cent). This represents a decrease from 53 per cent reached in 2005 and may reflect the more difficult conditions under which UNCDF works and the type of institutions it targets. The fact that FSPs sometimes experience repayment problems emphasizes the need to address those challenges quickly, before they spiral out of control. Building institutional capacity for stronger portfolio monitoring and repayment is a key focus of UNCDF support and will be closely monitored in 2007, with the target to restore the previous level of portfolio at risk at 30 days below 5 per cent.

25. Performance was strong in terms of investments made in local financial sector infrastructure (outcome 2.4). All the countries supported now have national microfinance associations and networks of FSPs. In fact, 22 out of 28 FSPs funded by UNCDF belong to a national association or network. Those two results clearly show the recognition by the FSPs of the importance of collaboration and joint representation to (a) strengthen their advocacy capacity towards national authorities; (b) agree on common standards; and (c) share lessons and experiences based on sound microfinance practices. In eleven LDCs, UNCDF provided direct support to strengthen the institutional capacities of the national associations, either in the form of grants or by ensuring their inclusion in training activities and the elaboration of national strategies. As the sectors develop, other indicators will be added to measure progress at the meso level.

Table 6. Achievement of 2006 targets in the microfinance practice area

Core results and outcomes	Overall target achievement in 2006 (%)	Performance achieved
Core result: established sustainable retail intermediaries providing a range of financial services to low income households		
Outcome 2.1: Increased outreach of UNCDF-supported financial intermediaries to low-income households	Target: 586 941 clients Result: 616 035 clients	Exceeded targets
Outcome 2.2: Increased breadth and depth of services provided by UNCDF-supported financial intermediaries to low income households	*	*
Outcome 2.3: Increased sustainability and efficiency of UNCDF-supported financial intermediaries serving low-income households	4/8 FSPs or 50% ** (Profitability) 11/28 FSPs or 39% (Portfolio quality)	Partly achieved Below expectations
Core result: supporting industry infrastructure for delivery of financial services to low-income households established		
Outcome 2.4: Local financial sector supporting infrastructure in place	12/12 countries or 100% 22/28 FSPs or 78.6%	Fully achieved
Outcome 2.5: Increased visibility and transparency of UNCDF-supported financial institutions	14/28 FSPs or 50%	Partly achieved
Core result 3: Enabling environment for building inclusive financial sectors fostered		
Outcome 2.6: Increased capacity of government to support conducive policy environmnent for an inclusive financial sector	12/10 countries or 120%	Exceeded targets
Outcome 2.7: Increased capacity of regulatory and supervisory authorities to develop conducive legal framework for an inclusive financial sector	12/9 countries or 133%	Exceeded targets
Outcome 2.8: Nationally-owned government and donor strategies exist in support of building inclusive financial sectors	5/6 countries or 83%	Fully Achieved
Total	**78 %**	**Fully Achieved**

* Reporting on outcome 2.2 will be captured by the national household surveys that UNCDF expects to carry out in partnership with the World Bank under the Data Project which UNCDF and the World Bank are currently structuring. Reporting of results will take place after baseline and follow-up surveys have been completed.

** Only 8 out of 28 FSPs had reported on this indicator by end of March.

26. Only half of the FSPs that UNCDF supported had industry standard audits or ratings (outcome 2.5). This further reflects the challenging niche where UNCDF is working, namely, start-up and emerging institutions. It also reflects the fact that UNCDF is working almost exclusively in LDCs with weak and highly constrained financial sectors, including several post-conflict countries. Many of these countries do not have the necessary capacity to audit FSPs. Building the capacity for audit standards recognized by the Consultative Group to Assist the Poorest (CGAP) is therefore a key element of sector development programmes and will be actively promoted in the future.

27. All eleven programme countries have seen improvements in their policy and enabling environment for microfinance with support from UNCDF (outcome 2.6). The strong achievement at the policy level confirms the impact of UNCDF at the policy level in all countries where UNCDF has promoted the inclusive financial sector approach.

28. The UNCDF financial sector development approach builds the capacity of national policymakers to develop national strategies for inclusive financial sectors. A constraints-based approach to policy issues builds the capacity of policymakers to identify constraints to inclusive finance and to then remove the most serious constraints (outcome 2.7). The strong

achievement on outcome 2.7 is a result of UNCDF support to training and capacity-building of regulatory and supervisory authorities.

29. Almost all active sector development programmes have developed joint government and donor strategies (outcome 2.8). That percentage increased from 66 percent in 2005 to 83 per cent in 2006 as more countries completed their consultative processes. In five countries, the implementation of the inclusive finance action plans has commenced.

29. Two further initiatives have contributed to the process of building inclusive financial sectors: the United Nations Advisors Group on Inclusive Financial Sectors and the Dakar Conference on Financial Inclusion.

30. The United Nations Advisors Group on Inclusive Financial Sectors, hosted by UNCDF, initiated its work in 2006. It held two meetings that resulted in the formation of several working groups on advocacy, private sector engagement, regulatory issues and research and knowledge-sharing. Each working group has already defined its working agenda including the following: holding a series of regional conferences on regional issues concerning financial inclusion and regulation during late 2007 and 2008; launching five country studies with appropriate models to engage the private sector in financial inclusion; raising public awareness on the importance of financial inclusion among governments, central banks and policy makers; and advocacy and cooperation with the World Bank on developing instruments, methodologies and pilot studies to measure access to financial services.

31. UNCDF and UNDP co-organized the United Nations Conference on Financial Inclusion in June 2006 in Dakar. It gathered 320 high-level participants from governments, central banks, multilateral and bilateral donors, private sector, financial service providers and their networks, from 53 countries including 48 African countries. The Conference adopted the Dakar Declaration on Building Inclusive Financial Sectors in Africa and established a Steering Committee to support and follow up the implementation of the Dakar Conference recommendations. This Conference and its outcome highlighted the convening power of UNCDF and UNDP around the theme of inclusive finance and created a powerful platform for advocacy, knowledge sharing, learning and partnership development to enhance sustainable access to financial services in Africa. The steering committee to follow-up the recommendations of the Dakar Conference met in early 2007.

32. Lastly, it is useful to mention the results related to the UNCDF role as the policy and technical advisor to the UNDP family on issues related to microfinance to ensure consistent application of best microfinance practices. In 2006, UNCDF supported UNDP inclusive finance activities in seven non-LDCs in Africa under its joint regional programme with the Regional Bureau for Africa. UNCDF continued to work with UNDP to implement the action plan to follow up on the recommendations to UNDP from the CGAP peer and portfolio review processes. As part of the implementation of the UNDP microfinance policy, which was published in January 2006, UNCDF works closely with each of the regional bureaux of UNDP to ensure adherence to this policy and thereby the quality of UNDP programming in microfinance around the world.

33. The above analysis reflects the comparative advantage enjoyed by UNCDF and UNDP in working jointly towards ensuring sustainable access of low-income households and small enterprises to a broad range of financial services. In all LDCs their field presence has allowed the two organizations to play an active advocacy role and provide capacity-building to governments and other stakeholders in establishing policy, legal, and regulatory environments conducive to inclusive finance. The investment mandate of UNCDF has enabled the two organizations to make necessary investments through loans and grants to FSPs, thereby ensuring a rapid growth in their outreach capacity. As a result, the UNDP strategic plan, 2008-2011, contemplates that UNDP and UNCDF will expand the geographical scope of their joint interventions in inclusive finance, thus contributing to the promotion of inclusive growth and the reduction of poverty.

II. Management results

C. Performance analysis for sub-goal 3: organizational performance

34. The UNCDF performance framework for measuring organizational performance is derived from the framework used by UNDP for its balanced scorecard for country offices. As is the case for UNDP, performance is measured according to four different perspectives: learning and growth, client satisfaction, internal efficiency and financial resources. For each perspective a number of strategic objectives have been identified. These correspond to the UNCDF management plan and to specific indicators that measure and the achievement of performance targets. Each strategic objective is accompanied by indicators and targets that were established at the beginning of 2006.

35. Table 7 provides on overview of 2006 results on organizational performance. The overview contains about half of the strategic objectives and indicators used in the UNCDF balanced scorecard, the balance being used mainly for internal management purposes.

Table 7. Achievement of 2006 targets for organizational performance

Perspective	Strategic objective	Indicator	2005 result	2006 target	2006 result
Learning and growth	Expand geographically to more LDCs, including post-conflict LDCs	LDCs with UNCDF programmes (> $50,000 investment/year)	26 LDCs	32 LDCs	28 LDCs
		Post-conflict LDCs with UNCDF programmes	13 LDCs	15 LDCs	13 LDCs*
	Increase average investment size	Investment per LDC per year	$0.72 million	$1.1 million	$0.85 m
Client satisfaction	Improve strategic partnership with UNDP and the rest of the United Nations system	UNDP country office satisfaction with overall quality of partnership with UNCDF	73%	80%	TBD***
Internal efficiency	Increase staff at regional and country level to be closer to clients and investments	Ratio of professional staff posted at country and regional levels	63%	75%	71%
	Strengthen United Nations coordination	Integration of UNCDF in United Nations country-level programming framework	26 LDCs	32 LDCs	28 LDCs
	Improve efficiency of delivery	Administrative-to-total-expenditure ratio	32%	26%	22%
		UNDP CO satisfaction with timeliness of operational support	64 %	80%	TBD***
	Strengthen 'people management'	Staff perception	65%	75%	70 %
Financial resources	Achieve resource mobilization targets	Core resources mobilized	$9.5 million	$18 million	$13.9** million
		Non-core resources mobilized	$10.3 million	$18 million	$8.1 million
	Ensure delivery against plan	Delivery against approved annual spending limits	74%	90%	84%

* Based on comparison of the 2005 and 2006 LDC lists.

** Includes a 2005 core contribution of $1.2 million which was received and recorded as income in January 2006.

*** Results of surveys in these areas had not yet been received by the time this report was finalised. They will be included when available.

36. In 2006, UNCDF had ongoing programmes with investments of $50,000 or more in 28 LDCs, including all of the post-conflict LDCs in which it had been active in 2005. The total number of programmes with UNDP grew to more than thirty, reflecting the deliberate

choice of UNCDF to programme together with UNDP. The average UNCDF expenditure per LDC increased by 18 per cent in 2006, to $0.85 million. That reflects the improved overall programme delivery against core resources in the local development and microfinance practice areas. The increased programme delivery was facilitated by the mainstreaming of the UNCDF administrative budget into the UNDP biennial budget, which ensured that all UNCDF core income could be used for programme expenditures.

37. Organizational performance was least satisfactory in the area of financial resources, both in terms of core and non-core resources mobilized. Despite the continued excellent performance record of UNCDF and enhanced resource mobilization efforts that began in late 2005, a variety of factors constrained its ability to meet its resource mobilization targets in 2006. Those factors related primarily to continued focus among donor Member States on United Nations reform and uncertainties related to the work of the High-level Panel during much of 2006. Those issues created concern among some donor member states regarding UNCDF and its role within the UNDP development framework. In addition, limited experience and guidance within the United Nations system with respect to joint programmes and joint resource mobilization resulted in several donor Member States channelling funds intended for UNCDF through UNDP, which funds are not considered 'non-core resources' for UNCDF. Further, UNCDF was not able to hire its business development advisor until April 2006, and was thus delayed in implementing some significant aspects of its resource mobilization programme – particularly at country level – until the second half of 2006.

38. Core resources increased from $9.5 million in 2005 to $13.9 million in 2006, an increase of 46 per cent, including a core contribution of $1.2 million for 2005 that was received and recorded in early 2006. If that core contribution had been considered as a contribution in 2005, core contributions in 2006 would have increased by $2 million over 2005, an increase of 19 per cent. The increase is primarily a result of (a) a 40 per cent increase in new core donor Member States, and (b) sustained or increased contributions from existing core donor Member States.

39. With respect to non-core contributions, approximately $1 million that was designated for UNCDF activities was contributed to UNDP rather than as non-core contributions to UNCDF. If that amount had been received by UNCDF, non-core resources for 2006 would have been $9.1 million, approximately 12 per cent less than 2005. With increased capacity and tools in place for business development and resource mobilization, preliminary predictions indicate that the trend since 2003 of increasing levels of non-core contributions will continue in 2007. UNCDF notes, however, that both core and non-core resource mobilization was significantly below the $18 million targets set for both types of resources in 2006 due to the factors set forth above.

40. In the area of internal efficiency, UNCDF was able to improve its efficiency of service delivery by reducing the ratio of administrative expenditures to total expenditures from 32 per cent in 2005 to 22 per cent in 2006. That improvement was due to several factors, including a rapid decentralization of professional staff to be closer to LDC clients and significant reductions in headquarters staff as part of the reorganization process begun in 2005. By the end of 2006, 71 per cent of UNCDF professional staff were posted to the country or regional level, and UNCDF had moved closer to UNDP physically by expanding its presence in the UNDP regional service centres in Dakar, Johannesburg and Bangkok. UNCDF is still addressing some of the unplanned consequences of the change management process, including the high workload associated with serving a larger number of LDCs and country level programmes with substantially reduced headquarters staff.

41. Staff perception, an indicator used by both UNDP and UNCDF to measure overall staff satisfaction through the global staff survey, stood at 70 per cent, which is a 5 per cent improvement compared to the 65 per cent score of 2005. There was strong evidence of the continued commitment of UNCDF staff to the mission and activities and UNCDF, in a transition year after the difficult change management process of 2005.

III. Financial analysis

42. As indicated above, total core income in 2006 was $13.9 million. Total income from core and non-core resources for 2006 was approximately $22.0 million, compared to $19.8 million in 2005, an increase of approximately 11 per cent. Total income for 2006 increased to $27.2 million from $24.2 million in 2005 an increase of approximately 12 per cent. Of that increase, about $1.1 million was due to an increase in interest income.

43. Table 8 contains key information concerning UNCDF expenditures for the period 2001-2006. In 2006, there was a substantial increase in core programme expenditures compared to 2005. Core expenditures increased from $11.6 million in 2005 to $16.8 million in 2006. Overall non-core expenditures increased as well, combining a substantial increase of country-level non-core expenditures and a sharp reduction in non-core expenditures at headquarters in 2006 due to the completion of the International Year of Microcredit (YoM). Non-core expenditures made up 39 per cent of country level programme expenditures and one-third of total programme expenditures.

44. UNCDF was able to reduce its headquarters expenditures to $4.6 million in 2006 as compared to $6.7 million in 2005, a reduction of about 34 per cent. That reduction was largely attributable to the successful reorganization and change management process described above. 90 per cent of the UNCDF headquarters administrative budget was funded through the UNDP biennial budget. The remaining 10 per cent reflected 2006 costs associated with the UNCDF change management process, which were financed from UNCDF core resources.

Table 8. Expenditure trends, 2001-2006 (in millions of dollars)

Expenditures	2001	2002	2003	2004	2005	2006
Programme expenditures	$33.9	$24.8	$21.1	$22.9	$19.2	$25.2
- of which core	32.3	22.6	16.3	14.9	11.6	16.8
- of which non-core	1.6	2.2	4.8	8.0	7.6	8.4
Headquarters expenditures	6.0	5.5	6.2	5.3	6.7	4.6*
Total	**$39.9**	**$30.3**	**$27.3**	**$28.2**	**$25.9**	**$29.8**

Source: Financial statements for UNCDF

** This includes $4.2 million in expenditures against the UNDP biennial support budget allocation for UNCDF and $0.4 million against UNCDF core.*

45. Table 9 shows that in 2006 the Africa region accounted for 73 per cent of total UNCDF expenditures at the field level. Total expenditures in Asia grew to 16 per cent and are expected to grow further in 2007, with the start-up of a number of new UNCDF programmes in both local development and inclusive finance. UNCDF spent $1.2 million on its research and development agenda, focusing on knowledge management and developing new product innovations. About $0.3 million in non-core expenditures related to the final activities of YoM and the start-up on the United Nations Advisors Group on Inclusive Financial Sectors.

46. Overall, $20.8 million in programme expenditures (83 per cent) was spent at the country level, $2.9 million for country support provided from the regional level (11 per cent), and $1.5 million (6 per cent) at the headquarters level. Capital investments, either local development investments under the local development practice area, and investments in FSPs under the microfinance practice area, made up about two thirds of country-level expenditures and 54 per cent of total UNCDF programme expenditures.

Table 9. Programme expenditures per region and practice area (in millions of dollars)

Regions/specific purposes	Local development	Microfinance	Total
Africa	$ 13.7	$ 3.7	$ 17.4
Asia	3.8	0	3.8
Arab States	0.9	0.2	1.1
Latin America	1.4	0	1.4
Research and development	0.8	0.4	1.2
U.N. Advisors Group/YoM		0.3	0.3
Total	**$ 20.6**	**$4.6**	**$ 25.2**

47. Regarding its liquidity and reserve position at the end of 2006, UNCDF maintained its operational reserves at $22.6 million, the same level as 2005. In addition, total unexpended resources increased from $37.5 million in 2005 to approximately $38 million at the end of 2006. Accordingly, UNCDF was able to accomplish the development, management and financial results set forth above while sustaining its liquidity and financial soundness.